Noted by DD/I
15 Nov 1959

November 14, 1959

Dear Bill:

Vance Brand has shown me your letter regarding the new DLF policy, placing primary emphasis on the procurement of US goods and services where foreign exchange costs of development projects are involved.

I am in full agreement with his replies to the questions posed in your letter, and I wish to use this opportunity to reply to one of your questions which Mr. Brand was not in a position to answer, namely that regarding the procurement policy of ICA.

Let me say first that the operations of DLF and ICA are very different. DLF provides long-term development assistance. DLF loans for the foreign exchange costs of development projects are largely spent for capital equipment which should properly be financed on the basis of long-term loans. The Western European countries who are in a position to join with the US in providing such equipment are now financially able to provide the necessary long-term financing for their own products if they so desire. The new DLF policy is expected to promote such financing by European suppliers of capital equipment. The same considerations apply, although to a somewhat lesser degree, to Japan's ability to finance capital equipment.

ICA assistance, on the other hand, is primarily designed to provide basic economic strength to countries of importance to the United States. Defense Support assists those countries carrying heavy military burdens in the defense of the free world, and Special Assistance helps other countries where US interests require special aid programs. These programs are largely accomplished by the furnishing, on a grant basis, of industrial raw materials and other consumable commodities.

In view of the nature of ICA assistance, the adoption by ICA of a policy similar to the new DLF policy could not be expected to stimulate additional financing by other industrialized countries, since they are not in a position to undertake large-scale additional grant programs.

In addition, the ICA programs are handled largely through private trade channels and contribute substantially to the development of private enterprise in the newly developing countries. If US procurement were to be required for these consumable items, the recipient governments would have to work out a system of subsidies which would lead to governmental controls inimical to our objective of promoting free private enterprise.

Finally, a significant amount of ICA offshore procurement takes place in the newly developing countries themselves where it serves the purpose of furthering the development of such countries, thereby lessening their need for assistance from the United States.

We have just completed a review of the world-wide procurement policies of the ICA which, like the financial policies of other agencies of the Government, are always subject to re-examination. For the reasons stated above, we do not for the present contemplate basic changes in ICA procurement policies. We do, however, recognize the desirability of transferring from the ICA to the DLF, to the greatest extent possible, assistance which ICA grants in the form of help to specific development projects. We intend to move in this direction. Projects so transferred would then be financed under the new procedures of the DLF.

If you desire any additional information on this subject or on any other aspects of the new DLF policy, I will of course be glad to meet with you at your convenience.

Sincerely yours,

/s/ Douglas Dillon

Douglas Dillon

The Honorable J. W. Fulbright
United States Senate

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DEVELOPMENT LOAN FUND

November 13, 1959

Dear Senator Fulbright:

Your letter of October 22, 1959 requests a statement of the reasons for, as well as answers to nine questions about the recent procurement policy announcement by the Development Loan Fund.

The answers to these questions, which have been approved by the DLF Board, are attached. We welcome this opportunity to present our views by elaborating on the reasons for our new policy and indicating how it is designed to promote the overall foreign and domestic interests of the United States.

The policies and programs of the DLF must be responsive to changes in the environment in which it operates. Recently, it has become abundantly clear that the world in which the DLF began operations has changed.

Today, most other industrial nations are in a financial position also to provide long-term financing for the less developed countries. All important indicators of economic strength -- total production, per capita consumption, financial reserves -- have risen substantially in the industrial countries and are still rising. For some time the other industrialized countries have been supplying increasing amounts of capital equipment to the less developed countries. Such countries now also have the ability to finance their goods on terms suitable for countries in the early stages of economic growth.

Recognizing this, the United States has for some time been urging the industrial countries to extend long-term credits to the less developed countries. It is believed to be in their interest as well as ours that the pattern of world finance move toward a situation in which countries whose capital equipment and other related goods are in demand provide a larger share of the financing for their exports, thus relieving the United States balance of payments of some of this financing effort. We are sure you agree that good creditor policies which have long been followed by the U. S., now seem to be in order for other countries, both in the field of liberalizing trade and in the field of liberalizing finance.

The other major change which prompted the new DLF procurement policy was the substantial international payments deficit the United States has incurred over the past years and is still incurring. In this situation we feel that it is not necessary to use DLF funds to finance long-term capital exports from other strong industrial countries especially when they now are able to provide such long-term financing themselves.

The payments situation is discussed in some length in response to your first two specific questions. The basic problem is that, as a result of its balance of payments deficit, the United States is now losing gold and short-term dollar assets at an annual rate of almost $4 billion. Deficits of this magnitude, of course, cannot continue. It is hoped to deal with this situation in a manner consistent with a rising volume of trade. Domestic fiscal and monetary policies directed towards financial stability, including a balanced budget in the current fiscal year, have been adopted. These measures have contributed to the soundness of the U.S. economy and currency. The reduction of the balance of payments deficit to proportions consistent with a healthy world trade, however, requires action by other countries as well. The new DLF policy contributes towards this objective.

In so doing we are carrying out the obligations imposed on us by Congress in Section 202(b) of the Mutual Security Act which requires that we implement the program so as to avoid adverse effects on the U.S. economy. As indicated in Section 413(c) of that Act, this includes our balance of trade position.

The action on DLF procurement is but one of a series of developments which will operate to reduce our payments deficit. The United States has been urging countries to eliminate their discriminatory restrictions against U.S. exports. Every day brings news of encouraging action by some foreign country along these lines.

It is not only unfortunate but erroneous for the DLF decision to be construed as a new "Buy American" policy. If a loan applicant desires long-term financing to procure equipment abroad it is the DLF view that he should, when funds are not available from other international lending sources, look principally to the producing country to supply such funds on reasonable terms and conditions rather than to the DLF. Because of the presumption that offshore procurement can be financed abroad, the DLF will now give primary attention to providing, in accordance with its criteria, development loan financing for those applicants who wish to buy goods and equipment of U.S. origin. Whether they buy in America, however, is a question of choice, a situation made possible by the improved financial position of other industrialized countries.

Therefore placing primary emphasis on the financing of goods and services of U.S. origin constitutes, in light of the world payment situation, a policy well designed to advance U.S. interests at home and abroad. It specifically reflects the present situation characterized by the new found ability of other industrial countries to provide long-term financing for their own exports and by increasing foreign gains of gold and dollars from the United States. These are matters bearing importantly on our own economic well-being and therefore we have welcomed the opportunity to present our views. Undersecretary Dillon, the Chairman of our Board, and I, are ready, of course, to discuss this subject with you at your convenience.

With best wishes,

Sincerely yours,

(Signed) Vance Brand
Vance Brand
Managing Director

Attachment.

The Honorable
J. W. Fulbright
Chairman, Committee on
Foreign Relations
United States Senate

ATTACHMENT

ANSWERS TO SENATOR FULBRIGHT'S NINE QUESTIONS ON DLF PROCUREMENT POLICY

1. Why is an unfavorable balance of payments considered by the Administration to be an unexpected and unfortunate thing under present international economic conditions?

A balance of payments deficit is not new for the United States. Since 1950, we have had a deficit every year, except for 1957. What is new and was partly unexpected was the large size of the deficit in 1958 followed by an even larger deficit this year.

The balance of payments deficit which the U.S. incurred in previous years had beneficial aspects. It has contributed to the greatly improved economic and financial position of the rest of the free world. It has resulted in a healthy redistribution of financial reserves. This is encouraging foreign countries to make substantial reductions in their restrictions against dollar exports. We hope to see all discriminatory restrictions on trade eliminated in the near future. In addition, the increase in the financial reserves of the industrial countries has given them the ability to join with us in contributing to the economic growth of the less developed countries.

It must be recognized that if deficits were to continue, they could create important difficulties for this country.

Foreign governments do not watch the U.S. undergo large balance of payments deficits indefinitely without concern. What they are fundamentally concerned about is whether our country retains enough self-discipline to reduce its losses on international account before events force unfortunate policies upon us.

This quality of self-discipline, moreover, is exactly what we must also have as a leader of the Free World. Such discipline, among other things, implies that we will make a real contribution out of our own resources to the economic development of the less-developed countries. We cannot do this indefinitely by building up short-term foreign claims against diminishing gold reserves. Over any sustained period we must do it in the form of an excess of exports of goods and services over imports. Only in this way can we make a solid contribution to the strength of the Free World, without weakening our own position.

2. Has the trend toward an unfavorable balance of payments, which was of concern last spring, continued unabated? How long will this trend continue?

Our balance of payments has continued to show a deficit through the third quarter of this year. The loss of gold and liquid dollars was $840 million in the first quarter, $1,162 million (excluding the $1,375 million increased quota payment to the International Monetary Fund) in the second quarter, and, on the basis of preliminary figures, over $1,200 million for the third quarter. The gold and dollar loss figures for 1959 would be even greater in the absence of some large debt prepayments by other industrialized countries which ordinarily would have repaid their debts over a period of years in accordance with the servicing schedule. For example, in October the United Kingdom made a $250 million prepayment on a loan by the Export-Import Bank and this prepayment will serve to reduce the fourth quarter gold and liquid dollar loss.

The decline in exports between the second and third quarters was much less than the usual seasonal decline and third quarter exports were higher than the level of the third quarter of 1958. While imports tended to level off between the second and third quarters, the level of imports is at an all-time record high. Improved economic conditions overseas and the continued progress toward the elimination of discrimination against U.S. exports should serve to strengthen our export position. At the same time, there are indications that the rate of increase in our imports will be substantially lower.

The current deficit reflects the continuation at high levels of U.S. public and private capital outflows and military expenditures abroad at the same time that our export surplus of goods and services has declined.

Because of the notable uncertainty of balance of payments forecasts due to the many unpredictable elements involved, it is not possible to arrive at any definite judgment as to when the current unfavorable trend in our payments will be terminated.

3. Will the change in DLF policy have an appreciable effect on the U.S. balance of payments?

Because implementation of the policy is only beginning the immediate impact on the balance of payments will not be large, but this impact will increase in time and become particularly significant as a higher level of DLF disbursements of new loans is achieved annually. You will recognize that the long term effect on the U.S. balance of payments cannot be stated with any precision since such an estimate would have to be based on future availability of resources to the DLF which only the Congress can decide.

At any rate the effect of the change in DLF policy on the U.S. balance of payments should not be appraised in isolation. It is one step which the Government has taken in light of our payments position. While the estimated effect of the change in DLF policy is in itself not insignificant, the total effect of our policies in conjunction with the actions of other governments in removing their trade discrimination and liberalizing their financing should have an appreciable effect on the balance of payments.

4. Does this policy change encourage or discourage the tendency of American industry to "price itself out of the world market"? What is your estimate of the value of the subsidy to U.S. producers which would be involved over the next five years in the new DLF policy?

The new policy is not intended to protect or to provide subsidy to American industry. To attract purchasers American industry must continue to compete with producers in other industrialized countries, for the fact that the DLF will give primary emphasis to financing goods and services procured in the United States is no assurance that purchasers will choose to buy here. It is up to American industry to stimulate that choice by making attractive to buyers the products and facilities it offers.

American industry as a whole has not priced itself out of the world market. The United States cannot, of course, be complacent, for even now many instances exist where some products of segments of American industry are having difficulty competing abroad. Our prices on many products, however, are competitive, particularly when viewed in the context of a total sales package including price, quality, reliability, availability, guarantee, terms, delivery, service, and inventory for re-order. These factors, when taken together, can make American equipment very attractive. It is hoped that more buyers from the less developed countries will come to learn of the intrinsic merits of such a package. The new DLF procurement policy may well serve to acquaint more of them intimately with what American industry has to offer and what it can contribute to their development.

When the United States exports developmental products of American origin we are also exporting technical know-how and other attributes of the American way of life. These are important facets of our economic system which have contributed to our own strength and well-being and can increasingly advance the American economic philosophy abroad. The new DLF policy should facilitate greater participation by American private enterprise in development abroad.

5. Has it not been the policy of the United States heretofore to promote multilateral trade, rather than bilateral trade, and does this not amount to a radical change of policy?

It has been, and continues to be, the policy of the United States to promote multilateral trade. A distinction may be drawn, however, between policies and programs for achieving multilateral trade and those special loan operations undertaken to finance economic development abroad. DLF loan operations, while furthering trade, are designed primarily to provide capital equipment and services not otherwise available to the borrower from existing sources of financing or as a result of their normal international trade. The new DLF policy goes hand in hand with other efforts by this Government to persuade other prosperous nations to assume more responsibility in financing the development of the less developed countries of the Free World. Increased development abroad is an important prerequisite to greater and sustained multilateral trade. Further assistance efforts by others, and continued efforts by ourselves, will contribute to this important policy objective. Placing primary emphasis on DLF financing of goods and services of U.S. origin cannot, under these circumstances, be regarded as a departure from a multilateral trade policy.

This Government has, in the past year, including the period when the DLF procurement policy was under review, undertaken many programs which directly or indirectly lend financial support to its multilateral trade policy. These programs, totalling many billions of dollars, involve the provision of additional funds for international lending agencies such as the International Bank for Reconstruction and Development, the International Monetary Fund, the Inter-American Development Bank, and the Mutual Security Program. The Government, of course, has also continued its active support of the General Agreement on Tariffs and Trade (GATT). These steps indicate further that the new DLF policy certainly intends no radical change on the part of the U.S. Government.

6. Have not the recent moves of Western European countries to lift restrictions on U. S. imports served both to alleviate the problem and to advance the policy of trade liberalization? How will such countries react to a seeming negation of that policy?

It is true that the recent liberalization moves of the Western European countries should help to alleviate our international payments problem as well as contribute to the healthy growth of world trade and income. These countries can go, and intend to go, further. We hope in the near future that they will eliminate all remaining discriminatory restrictions to trade.

The new DLF policy works in the same direction of helping to bring our international accounts into a satisfactory balance.

Europeans understand the basis for our DLF policy. Loans by the Development Loan Fund are intended to make it possible for the less developed areas to acquire goods which they would not otherwise be able to purchase, and hence would not enter into international trade in the absence of this special public financing.

The DLF policy is not in conflict with the policy of dismantling quota restrictions which hamper the free flow of trade. It will not be considered by European countries as a negation of that policy.

7. What other industrialized nations making development loans do, or do not, tie their loans to purchases of goods and services of domestic origin?

For various reasons, whether through export credit facilities or other formally tied financing arrangements, through traditional marketing arrangements, through discrimination against other country's exports, or through other factors, the bulk of the development financing provided by other industrialized countries is used to buy their own products or those of the monetary area of which they are the center.

8. Which members of the DLF Board, if any, did not agree that the changed policy is the one best calculated to promote the overall foreign and domestic interests of the United States? Is ICA going to adopt a similar policy?

In arriving at this policy members of the DLF Board discussed the matter from different viewpoints. Procurement is but one of the policies involved in advancing U.S. interests. The undertaking of the new policy was very carefully considered by the members of the highest level of the Executive Branch as well as by members of the DLF Board. It was approved by each member of the Board.

The announcement of the new policy, of course, relates only to the DLF, the agency for which I have responsibility. I cannot, therefore, speak for the ICA.

9. Inasmuch as the DLF will now be engaged primarily in promoting the export of goods and services of U.S. origin, would it be reasonable to absorb the activities of the DLF in the Ex-Im Bank?

The primary purpose of the DLF, as stated in the Mutual Security Act, is to foster long-term economic growth in the less developed areas by assisting the efforts of free peoples to develop their economic resources and to increase their productive capabilities. The new policy in no way changes this fundamental concept. The principal purpose of the Export-Import Bank, as indicated in its statute, is "to aid in financing and to facilitate exports and imports and the exchange of commodities between the United States . . . and any foreign country . . ."

The DLF is an instrument of U.S. foreign policy and its Board of Directors is by law "subject to the foreign policy guidance of the Secretary of State."

Another important fundamental difference is that DLF operates largely in countries who do not have dollar debt servicing ability sufficient to use the Export-Import Bank or other sources of finance to meet in whole or in part their development needs. Accordingly, DLF has used the technique of accepting currencies other than dollars in repayment. The DLF consequently is able to operate in such important friendly countries as Korea, Vietnam, Taiwan, Jordan, Somalia, Sudan, and Libya where the Export-Import Bank has not operated in recent years.

These, among other fundamental differences of purpose and approach of the two institutions, are the reasons they are separate entities. The new DLF policy does not in any way affect these basic distinctions. It should be noted, too, that the DLF financing of goods and services of U.S. origin is not a new development. Of the disbursements made through July 31, 1959 for which procurement source data is available ($49.5 million) about 56 percent were for procurement in the United States.